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BEFORE THE

POSTAL REGULATORY COMMISSION

WASHINGTON, D.C. 20268-0001

Review of Commission's Price Cap Rules	**Docket No. RM2013-2**

COMMENTS OF THE ASSOCIATION FOR POSTAL COMMERCE

Pursuant to Commission Order No. 1678, the Association for Postal Commerce ("PostCom") hereby submits these comments to the Postal Service's Notice of Proposed Rulemaking Requesting Comments on Proposed Commission Rules for Determining and Applying the Maximum Amount of Rate Adjustments ("Proposed Rules"), issued to "clarify the Commission's rules for determining and applying the maximum amount of rate adjustments in rate cases before the Commission and to improve other aspects of the process of adjusting rates for market dominant products." Proposed Rules at 1. While the Proposed Rules generally represent sensible changes to the Commission's Rules which simply conform the codified rules to reflect prior Commission decisions, several areas for improvement and clarification remain. PostCom submits these comments to highlight areas in which mailers and the Postal Service would benefit from additional refinement of the Proposed Rules. Specifically, PostCom urges the Commission to revise the Proposed Rules to clarify the treatment of promotional rates and to allow the Postal Service additional flexibility to consider trends in mailer behavior.

I. PROMOTIONAL RATES

The Commission's Proposed Rules regarding the treatment of temporary promotional rates and incentive programs have already been the subject of some controversy in Docket No. R2013-6. In particular, the Postal Service has raised the question of how, and whether, to apply these rules when it implements promotional or incentive pricing programs between regularly scheduled annual price changes. *See* United States Postal Service Notice of Market-Dominant Price Adjustment (Technology Credit Promotion), R2013-6, at 5 (claiming that the proposed rules in the present docket do not expressly provide for, but would allow, the Postal Service to offset a mid-year promotional decrease in rates with subsequent rate increases) ("Technology Credit Notice"). Contrary to the Postal Service's contention, PostCom believes that the Commission's current rules, and its Proposed Rule 3010.23(e), already address this scenario. The Commission could benefit mailers, however, by revising its proposed rules to clarify how mid-year promotions should be factored into the price cap to ensure that the Postal Service cannot create new cap authority through strategic timing of such promotions.

A. Mid-Year Promotional Rates Should Not Create New Cap Authority

The underlying principle that should guide the Commission in developing rules for promotional programs is that the Postal Service should not be able to create new price adjustment authority simply by implementing promotional pricing in-between regular price changes. PostCom suggests that there are two reasonable methods of achieving this goal. The first is to establish a default rule that volume sent under promotional programs be treated as if it was mailed at full postage for the purposes of calculating available rate adjustment authority. The second approach would be to treat adjustment authority created by promotional or incentive rates as unused rate adjustment authority available in the next price adjustment pursuant to existing and Proposed Rules 3010.26 and 3010.27, with the caveat that where negative authority results, that negative authority must be included in the adjustment calculations as prescribed by those rules.

1. Proposed Rule 3010.23(e)

The first approach would essentially codify the approach taken by the Postal Service and approved by the Commission with respect to the Summer Sale promotions approved in Order Nos. 219 and 439. Under this approach, the price adjustment calculation would "exclude the effect of the price decrease on the price cap for both future and current prices." Order No. 439 at 12; *see also* Order No. 219 at 9. As the Commission explained, "[t]he effect on the price cap is as if all the discounted incremental volume paid applicable full postage." Order No. 439 at 12. This approach is embodied in Proposed Rule 3010.23(e), which states that "[t]he Postal Service may exclude temporary promotional rates and incentive programs from its percentage change in rates calculations if the temporary promotional rates and incentive programs result in overall rate decreases." PostCom suggests that the Commission should establish this rule as the default method for accounting for temporary promotional rates and incentive programs, whether instituted during or between regularly scheduled price changes.

In approving the Summer Sales, which were authorized between annual rate adjustments in 2009 and 2010, the Commission specifically noted that the Postal Service's decision to treat all mail sent at incentive rates as if it had been sent at full price for purposes of cap compliance was reasonable because it ensured that mailers who were not eligible for the discounts would not be forced to pay for the discounts through higher prices in the future. *See* Order No. 219 at 10 (finding the approach reasonable because "[i]t shields mailers not eligible for the program from being charged higher rates based on the amount which otherwise would be banked from the program"); Order No. 439 at 12 (reaching the same conclusion because "ineligible mailers will not be charged higher rates based on the amount which otherwise would be banked from the program.") This protection of ineligible mailers is a significant benefit, ensuring that promotional rates benefit mailers as a whole (by increasing volume, reducing costs, and increasing total contribution) rather than favoring certain mailers at the expense of others, with no net benefit to the industry.

Establishing Proposed Rule 3010.23(e) as the default treatment of promotional and incentive rates also supports the Commission's stated goal in this rulemaking of providing "more certainty for the Postal Service and the mailing community as they make decisions that rely upon the Postal Service's authority to adjust rates for market dominant products." Proposed Rules at 1-2. Treating promotional volume as if it travelled at full rates eliminates the need to perform complicated calculations of rate adjustment authority. It establishes a simple rule that allows the Postal Service to focus on the operational and economic benefits of offering the promotion (*e.g.*, whether the promotion will increase mail volume), and it allows mailers to evaluate the promotion on its own merits. Whereas mailers, especially smaller mailers, are adept at evaluating whether a promotional price provides sufficient incentive to participate in the promotion, they may not have the tools or sophistication to make this same determination if they must also figure out how the promotion will factor into future price adjustments that may result in higher rates over the long term. Consequently, even if the Commission establishes true-up provisions and other protections, many mailers may decline to participate in promotions rather than undertake the time and expense to fully evaluate the potential benefits of the promotion. Proposed Rule 3010.23(e) simplifies the decision tree for mailers and will result in more effective promotions than a rule that allows the Postal Service to rely on the reduced promotional pricing to create additional price adjustment authority. This approach also simplifies the price adjustment rules overall by conforming the treatment of promotional pricing to the treatment of Negotiated Service Agreements under Proposed Rule 3010.24.

Accordingly, PostCom recommends that the Commission establish Proposed Rule 3010.23(e) as the default rule for calculating rate adjustment authority linked to promotional and incentive rates. Rather than state that the Postal Service "*may* exclude temporary promotional rates and incentive programs from its percentage change in rates calculations," the rule should state that the Postal Service "shall" take this approach unless it demonstrates good cause to account for promotional and incentive programs in another manner.

2. Unused Rate Adjustment Authority

Alternatively, the Commission could clarify that a mid-year promotional or incentive program that reduces rates could be treated as a decrease in rates creating unused price adjustment authority pursuant to Rules 3010.26 and 3010.27. If the promotional program is established between annual rate changes, Proposed Rule 3010.26(b) would determine how the unused authority is to be calculated. The Postal Service could then use this authority in accordance with Proposed Rules 3010.27 and 3010.28 as it sees fit.

PostCom believes that this approach is permissible under the Commission's current rules. In Docket No. R2013-6, however, the Postal Service argued that the rate authority stemming from a decrease in rates should be "delayed," allowing the Postal Service to apply additional authority in its next rate change, rather than "banked" as unused rate adjustment authority and applied according to Rules 3010.27 and 3010.28. The Postal Service was transparent about its motives at least, stating that it "does not wish to 'bank' the amount of the authority if such banked authority could be used only after it uses all authority banked previously, because the sum of previously banked authority and the new authority would be negative, and is likely to remain so until 2016." Technology Credit Notice at 5 n.3.

PostCom does not understand why rate authority created by a mid-year promotion—authority that will by definition be "unused" during the year—should be treated any differently than rate adjustment authority available, but not used, during an annual price adjustment. In both cases, rate adjustment authority is available, but not used. It should, therefore, be added to the "bank" of unused rate adjustment authority and used on a first-in, first-out basis as directed by existing and Proposed Rule 3010.27. The Commission should consider clarifying its Proposed Rules to state that rate adjustment authority created by a mid-year promotional rate decrease should be treated like any other unused rate adjustment authority.

B. Authority Related to Promotional Prices Should Be Tied to Products, Not Classes

To the extent that the Commission's final rules allow the Postal Service to create additional price adjustment authority through the establishment of mid-year promotional and incentive programs, the rules should clarify that any cap authority created should be applied only to those products which were eligible for the promotional or incentive rates. That is, the Postal Service should not be permitted to use any adjustment authority created to increase rates generally across a class. Instead, the additional adjustment authority should be tied to individual products. The Commission recognized this principle in Order No. 1541, allowing the Postal Service to account for revenue foregone from promotions only "so long as volumes are properly ascribed to the appropriate products." Order No. 1541 at 18

Such a rule is necessary to ensure that promotional pricing does not unduly discriminate against mailers not eligible for the discounted rates. If the adjustment authority is applied to the class generally, mailers who were not eligible for the promotion may pay higher rates as a result of the promotion. While PostCom supports the introduction of promotional and incentive pricing, such pricing should be part of a strategy to grow volumes and overall contribution, not simply a discount that favors one set of mailers at the expense of others. Limiting any adjustment authority created to the products eligible for the promotional and incentive rates—and to the products and volumes actually sent at that rate through true-up provisions—will ensure that promotional and incentive pricing is non-discriminatory.

C. True-up Provisions Needed

To the extent the Commission's rules allow the Postal Service to create or bank price adjustment authority based on volume sent at promotional or incentive rates, the Commission should require the Postal Service to reconcile the volume sent at promotional rates with the adjustment authority it claims in its next scheduled price adjustment. In Order No. 1541, the Commission expressed its concern that when including promotions in the price adjustment authority calculation, "if the volume weights used in the cap calculation are overstated, the price authority created would be overstated as well." Order No. 1541 at 17. Accordingly, the Commission approved the Postal Service's inclusion of revenue foregone from promotions in its price adjustment authority calculations only "so long as volumes are properly ascribed to the appropriate products." *Id.* at 18. Because the Postal Service relied on historical volumes that were likely to be smaller than the volumes that would actually be mailed at the promotional rates in question, the Commission approved the Postal Service's calculation. *Id.* at 17.

Requiring the Postal Service to true-up volumes sent at promotional rates in calculating its price adjustment authority during its next scheduled rate change would serve the same purpose. It would ensure that any changes in price adjustment authority reflect only volumes that actually travelled at promotional or incentive rates and that these volumes are attributed to the appropriate products. In doing so, it would protect against overstating the price authority created through promotions and incentives. *See* Order No. 1541 at 17.

II. ACCOUNTING FOR MAILER BEHAVIOR

In obtaining volumes for each rate cell, Proposed Rule 3010.23(d) would command the Postal Service to "make reasonable adjustments to the billing determinants to account for the effects of classification changes such as the introduction, deletion, or redefinition of rate cells." The proposed rule further directs that "adjustments shall be based on known mail characteristics" when possible. These provisions are reasonable, as they move away from a rigid, deterministic calculation and allow the Postal Service to account for well-supported changes that are likely to occur.

The rule further states, however, that "[a]djustments to billing determinants may not be based on anticipated changes in mailer behavior." This complete prohibition on relying on anticipated changes in mailer behavior is too restrictive. In certain instances, there may be well-defined trends in mailer behavior that clearly demonstrate that it is improper to use the most recent available 12 months of billing determinants as the rate cell volume. For instance, as PostCom explained in its comments in R2013-1 and ACR2012, changes in the behavior of mailers using the Standard Mail Flats product are likely to significantly influence that product's cost coverage and the impact of that product on the Standard Mail class as a whole. *See* Comments of the Association for Postal Commerce, Docket No. R2013-1 at 2-3; Reply Comments of the Association for Postal Commerce, Docket No. ACR2012 at 3-4. While PostCom recognizes that the Commission declined to account for mailer behavior with respect to Standard Mail flats in Order No. 1541, it nevertheless believes that it may be appropriate to account for mailer behavior in some instances. It is important for the Postal Service to take notice of demonstrable changes in mailer behavior and apportion its price adjustment authority accordingly. If the Postal Service ignores such changes while setting prices, it may inadvertently drive volume to less profitable categories or out of the system entirely, thus reducing overall contribution.

PostCom believes that a better approach would be for the Commission to evaluate adjustments made on the basis of anticipated changes in mailer behavior on a case-by-case basis. If the Postal Service can demonstrate that such changes are reasonably likely to occur, it should be permitted to account for these changes in determining volumes for particular rate cells. Conversely, if the Postal Service fails to adequately support its claimed adjustments, the Commission can reject the adjustment and order the Postal Service to use the standard billing determinants. The blanket prohibition contained in the proposed rule is too blunt an instrument for the complicated task of setting efficient prices that balance the demands imposed by the price cap and the dynamic needs of the mailing industry. Evaluating such adjustments individually preserves both the pricing flexibility granted to the Postal Service and the Commission's authority to ensure prices comply with the limits imposed by PAEA.

Respectfully submitted,

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